Stocktake on Financial Institutions’ Transition Plans and their Relevance to Micro-prudential Authorities

May 2023
The latest report by the United Nations Intergovernmental Panel on Climate Change underscores the urgency of taking more ambitious climate action. Global warming has already reached 1.1 degrees Celsius above pre-industrial levels and global greenhouse gas emissions have continued to increase. To limit global warming to 1.5 degrees, emissions will need to be cut by almost half by 2030, which will require rapid and far-reaching transitions across all sectors and systems.

The risks associated with the transition to a low emission economy, as well as the consequences from increasing physical risks, will affect all sectors of the global economy. This transition has the potential to significantly impact the safety and soundness of financial institutions and the stability of the global financial system.

Strengthening the resilience of the financial system to climate change risks and supporting the transition to a sustainable global economy is at the core of our mandate. Transition plans are a key tool for an orderly economy-wide transition and are increasingly receiving global attention from international standard-setters and voluntary market-led initiatives.

This report by the NGFS explores the relevance and extent to which financial institutions’ transition plans relate to micro-prudential authorities’ roles and mandates and whether they should be considered within their supervisory toolkit and in the overall prudential framework. It provides a comprehensive stocktake of current frameworks and literature on transition plans practices, as well as an overview of the current state of play in different jurisdictions.

The stocktake highlights the range of current frameworks for transition plans and differing perspectives on the role of the micro-prudential supervisor and underscores the need for greater coordination across regulatory agencies and standard setters. We suggest that any future supervisory guidance use a building block approach to recognize the spectrum of regulatory objectives and range of jurisdictional approaches.

We hope this report will provide a foundation for further collaboration and cooperation and serve as a call to action to all NGFS members, observers, and international standard setters to continue advancing the discussion on the role of transition plans in greening the financial system and the relevance of these plans to supervisors’ mandate, toolkit, and the overall prudential framework.

We genuinely appreciate the commitment and dedication of all workstream members who have contributed to this stocktake, as well as the valuable engagement of other stakeholders whom we have consulted in the past year. Our special thanks go out to the co-leads and the NGFS Secretariat.
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Transition plans have the potential to become centrepiece in showing the real economy’s pathway to a net-zero future. For financial institutions, transition plans can be viewed as an important part of the wider transition finance framework that supports efficient allocation of capital across sectors toward a low emission economy, as well as important tools to manage climate risks in a forward looking manner. Some jurisdictions view them as a necessary tool to help achieve their climate objectives, including net zero goals, and build resiliency in their respective economies.

Building on the conclusions of the NGFS Report on ‘Capturing risk differentials from climate-related risks’, the NGFS sought to examine the relevance and extent to which financial institutions’ transition plans (i) relate to micro-prudential authorities’ roles and mandates, and (ii) could be considered and used most effectively within their supervisory toolkit and in the overall prudential framework.

The work will be conducted in two phases. Phase 1 of the work programme consisted of two stock-take exercises, by way of (i) a review of available frameworks and literature on transition plans from external bodies, and (ii) an analysis on the current state of play in the regulatory landscape as it relates to transition plans among NGFS members. This report summarises these stock-take exercises, including six key findings and next steps for Phase 2 that the NGFS can take forward to advance the discussion on the relevance of transition plans and planning to micro-prudential authorities.

Key findings from Phase 1

Key finding 1: There are multiple definitions of transition plans, reflecting their use for different purposes

The review showed that there are multiple definitions of transition plans, reflecting their use for different purposes. Currently, there are a range of frameworks for transition plans and differing perspectives on the role of the micro-prudential authority in requiring, using, and enforcing transition plans. This reflects the range of jurisdictional approaches to addressing climate change, regulatory mandates, and financial system regulatory infrastructures.

The stylised transition plan use cases in the table below captures, at a high level, the potential orientation of these plans depending on jurisdictional requirements or expectations. Based on these use cases, the NGFS concluded that transition plans can broadly be categorised as either strategy-focused or risk-focused.

a) Strategy-focused plans primarily aim to provide transparency to external audiences on a firm’s strategic approach to meet specific climate targets.

b) Risk-focused plans have a narrower scope in content and application, focusing on the management of risks associated with real economy transition.
Key finding 2: There is merit in distinguishing transition planning (transition strategy) from a transition plan (transparency to a specific audience)

For the purposes of this stocktake, the NGFS distinguished ‘transition planning’ from a ‘transition plan’ by drawing a line between what is an internal process and what is an external-facing document.

a) ‘Transition planning’ is the internal process undertaken by a firm to develop a transition strategy to deliver climate targets and/or prepare a long-term response to manage the risks associated with a transition.

b) ‘Transition plans’ are a key product of the transition planning process and are mainly used as an external-facing output for external audiences (e.g. public stakeholders or supervisors) which represent the strategy of how firms plan to align their core business with a specific strategic climate outcome.

Transition planning can take place without the disclosure of an underlying, formal transition plan. However, transition plans are a useful tool which bring together aspects of the transition planning process to meet the needs and interests of a range of users, and may aid institutions in formalising and manage their internal transition planning.

Key finding 3: Existing frameworks speak to a mix of objectives, audiences and concerns for transition plans but predominantly relate to climate-related corporate disclosures

The review of existing literature showed that there are various regulatory objectives that could be advanced through the use of transition plans, which may include micro-prudential authorities’ objective to supervise financial institution safety and soundness, as well as other objectives related to financial stability, market integrity and conduct. Transition plans prepared using current available frameworks are primarily focused on corporate strategy and are intended to be used by a broader audience than those

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Categories of transition plan use cases

<table>
<thead>
<tr>
<th>Actor requiring transition plans</th>
<th>Government</th>
<th>Corporate</th>
<th>Financial Regulator</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulator objective</td>
<td>Climate outcomes (e.g., Paris Agreement)</td>
<td>N/A</td>
<td>Market conduct / consumer protection</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Financial Stability</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Safety and Soundness of financial institutions</td>
</tr>
<tr>
<td>What is the primary objective of the transition plan?</td>
<td>Achieve national climate outcomes through corporate action</td>
<td>Inform shareholdes and investors of a corporate's strategy in response to climate change and transition</td>
<td>Provide transparency to market actors e.g., maintain market integrity, prevent financial misconduct and/or greenwashing</td>
</tr>
<tr>
<td></td>
<td>Disclosure of strategy to meet climate targets</td>
<td>Disclosure of strategy to meet climate targets</td>
<td>Aggregate report on the potential build-up of climate-related risks in the financial system</td>
</tr>
<tr>
<td>What is the primary tool to achieve that purpose?</td>
<td>Disclosure of strategy to meet climate targets</td>
<td>Disclosure of strategy to meet climate targets</td>
<td>Report to supervisor on how the institution will manage climate related risks associated with corporate strategy</td>
</tr>
<tr>
<td>Who is the primary audience?</td>
<td>Public</td>
<td>Shareholders and investors</td>
<td>Market participants, consumers</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Macro-prudential regulators</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Micro-prudential regulators</td>
</tr>
<tr>
<td>Is the information publicly available?</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Jurisdiction-specific decision to determine whether it needs to make the information public to meet regulatory objectives</td>
</tr>
<tr>
<td></td>
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<td></td>
<td>Jurisdiction-specific decision to determine whether it needs to make the information public to meet regulatory objectives</td>
</tr>
</tbody>
</table>

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More Strategy Focused
Broader scope in content and application
Publicly available disclosure

More Risk Management Focused
Narrower scope in content and application
Not necessarily publicly disclosed
who are primarily focused on the financial risk-management aspects of the transition. While the information needs of a micro-prudential authority may be met by, for example, using transition plans disclosed as part of these disclosures, it is unlikely that the micro-prudential authority would be able to set the expectations based on transition plans that take a broader, strategic approach given its narrower focus on safety and soundness.

Key finding 4: Transition plans could be a useful source of information for micro-prudential authorities to develop a forward-looking view of whether the risks resulting from an institution's transition strategy are commensurate with its risk management framework.

Micro-prudential authorities seek to understand a financial institution's strategy to prepare/respond to the risks associated with climate change. Transition plans could help these authorities understand the transition risks an institution may be exposed to as a result of its strategy, risk appetite and corresponding risk management framework. 1

Transition plans can also be used to monitor and supervise financial institutions' short- and long-term strategies to manage climate-related risks, including those resulting from an institution who is off track from its transition plan, and understand how different transition pathways can affect its continued safety and soundness.

Key finding 5: There are some common elements to all transition plans which are relevant to assessing safety and soundness.

There are common elements to all transition plans which are relevant to assessing safety and soundness of the institution, such as governance, strategy, risk management and metrics. These common information points could inform the design of transition plan frameworks regardless of their thematic category or whether they are adopted by the micro-prudential authority, securities regulators, financial/climate reporting authority or alternate. The driver and context behind an institution's transition plan will play a key role in driving supervisory expectations and risk management considerations, as set out in the diagram below.

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1 Similarly, corporate transition plans provide financial institutions with valuable information on their counterparties’ future trajectory, which in turn can inform financial institutions' own strategy, risk appetite and risk management.

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Key finding 6: The role that micro-prudential authorities play needs to be situated in the context of the actions of other financial and non-financial regulators rather than acting in isolation

There are a number of potential uses for the information within transition plans that could meet different regulatory objectives, including those of the micro-prudential authorities, macro-prudential regulators, securities/market conduct regulators, as well as the government. Consequently, greater coordination across regulatory agencies and standard setters across financial and non-financial sectors, both within jurisdictions and internationally, is needed to leverage respective resources in assessing transition impacts from a transition and physical risk perspective. There also needs to be collaboration across supervisory jurisdictions and their institutions to ensure interoperability of transition plans, reduce regulatory fragmentation and related burden on firms and prevent “arbitrage” of different emissions regulations and interpretations of a transition plan amongst different users.

Next steps for Phase 2

Following the overall conclusion and key findings, the NGFS will take forward actions in two broad areas.

1. **Engagement with relevant international authorities and standard setters:** Given the different scope of transition plans as well as their potential relevance to the micro-prudential authorities, the NGFS will engage standard setting bodies, such as the FSB, BCBS, IAIS, and IOSCO, so that they can advance their respective work on transition plans and planning in a coordinated manner.

2. **Further actions by the NGFS:** Based on the findings of Phase 1, the NGFS will also take forward additional work to advance the discussion on the relevance of transition plans and planning to micro-prudential authorities’ mandate, supervisory toolkit, and the overall prudential framework.
Climate change and the transition to a low emission economy can affect the safety and soundness of financial institutions, the stability of the wider financial system, and the economic outlook. The risks associated with the transition to a low emission economy as well as the consequences from increasing physical risks affect all sectors of the global economy. This warrants detailed planning by corporates, using bespoke strategies and risk management frameworks, to build resiliency in the business models over the short, medium, and long term.

Transition plans have the potential to become centrepiece in showing the real economy’s pathway to a net-zero future. For financial institutions, transition plans can also be viewed as an important part of the wider transition finance framework, such as that set out by the G20 Sustainable Finance Working Group (SFWG), that supports efficient allocation of capital across sectors toward a low emission economy. Some jurisdictions view them as a necessary tool to help achieve their climate objectives, including net zero emission goals, and build resiliency in their respective economies.

The Taskforce on Climate-Related Financial Disclosures’ (TCFD’s) 2021 Status Report recommended the introduction of climate transition plans. The importance of transition plans is receiving global attention, from the G20, OECD and voluntary market-led initiatives such as the Glasgow Financial Alliance for Net Zero (GFANZ). In addition, as jurisdictions and financial institutions publicly commit to climate targets, there is growing focus on the need for credible and comparable plans, how firms will deliver on them as well as accountability mechanisms.

There is no consistent approach to whether transition plans address both the mitigation and adaptation aspects of transition. A transition to a low emission world will still give rise to both transition and physical risks. Micro-prudential authorities are concerned with the financial risks arising from climate change whether these are transition or physical risks. Accordingly, this paper uses transition plans in a broad sense as an articulation of a financial institutions’ approach to climate change and the transition to a low emission world, which encompasses both transition and physical risks.

This paper builds on the conclusions of the NGFS Report on ‘Capturing risk differentials from climate-related risks’, which underscored that micro-prudential authorities should focus their efforts on the forward-looking assessment of transition risks. To that end, the NGFS decided to explore the relevance and extent to which financial institutions’ transition plans relate to micro-prudential authorities’ roles and mandates and could be considered within their supervisory toolkit, as part of its new work programme.

**Understanding the role and responsibilities of micro-prudential authorities**

To understand the extent to which micro-prudential authorities should engage with financial institution transition plans, it is important to first recap the role and responsibilities of the micro-prudential authority (recognising the precise mandate and institutional setup differs between jurisdictions) and situate that in the context of other regulatory or climate objectives.

Micro-prudential authorities are focused on the safety and soundness of individual financial institutions. As it relates to climate risk management, micro-prudential authorities’ roles and responsibilities focus on supervising financial institutions’ climate risk management practices, such as through setting supervisory expectations and assessing financial institutions against those expectations, recognising that physical and transition risks are drivers of conventional prudential risks which could affect financial institutions’ safety and soundness.

This differs from other regulatory objectives, such as regulators with macro-prudential, market conduct/integrity, and consumer protection objectives, which can alter the

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2 In this stocktake report, the term ‘corporates’ is used to describe firms in the real economy, including financial and non-financial firms. Consistent with the mandate of the NGFS Workstream on supervision, ‘Financial institutions’ and ‘institutions’ are used to describe banks and insurers subject to micro-prudential supervision.


4 ‘Micro-prudential authority’ is used in this paper to refer to micro-prudential supervisory and regulatory authorities.
assessment on the relevance of transition plans and their purpose to these regulatory objectives.

Lastly, it is important to acknowledge there may be differences between jurisdictions’ approaches to transition to a low emission world. For example, while some economies are focused on emissions reduction, other economies may be more focused on sustainable development, enhancing resilience to climate change, or developing their economy while keeping emissions low consistent with international agreements. This, in turn, changes the context in what to expect from the approach to transition plans in different jurisdictions as well as how micro-prudential authorities may assess financial institutions' safety and soundness during the transition to a low-emission economy.

The relationship between financial institution and counterparty transition plans

Equally important to setting the stage for this phase of the NGFS’s work on transition plans is acknowledging that financial institutions do not operate in isolation, and that financial institutions will be both users of transition plans from corporates as well as preparers of their own transition plans. Ultimately, forward-looking information contained in transition plans developed by corporates will be key to enable the financial sector to mobilise private finance in support of the transition.

Financial institutions such as banks and insurers facilitate financial transactions in the real economy – they invest in, lend to, and underwrite insurance for corporates in all sectors. Consequently, how successful these institutions may be in preparing to respond to climate-related risks depend in large part on how well they manage and mitigate their exposures to these counterparties who are also preparing to respond to these risks. In the context of transition plans, it means that the extent to which a financial institution can credibly develop and implement its transition strategy is largely dependent on the extent to which its counterparties can credibly develop and implement their strategy, which forms the basis of counterparties’ and financial institutions’ transition plans. At the same time, financial institutions should not merely mirror passively the evolution of the real economy. Given the role of financial institutions as intermediaries in the real economy, if the financial institutions develop transition plans, they can also proactively, through their engagement, seek to support and drive their counterparties to transition to sustainable activities, that are compatible with the institutions’ business objectives and risk management practices.

The relationship between financial institutions and their counterparties’ transition plans should be further explored, also with regard to the micro-prudential authorities’ roles and mandates relative to the financial institutions’ transition plans.
2. Introduction to the NGFS’ work on transition plans

The objective of the NGFS is to examine the relevance and extent to which financial institutions’ transition plans (i) relate to micro-prudential authorities’ roles and mandates, and (ii) could be considered and used most effectively within their supervisory toolkit and in the overall prudential framework.

The work is organised into two phases:
• Phase 1 is the scoping phase where the NGFS undertook two stocktake exercises. The first was focused on a stocktake of available frameworks and literature on transition plans from external bodies, which was executed through a documents review. The second was focused on the current state of play in the regulatory landscape as it relates to transition plans, which was executed through a survey of NGFS members. This work, which forms the basis of this report, was conducted in the fourth quarter of 2022.
• Phase 2 is the action phase, where the NGFS intends to take forward next steps based on the outcomes of Phase 1.

This stocktake report summarises the work undertaken in Phase 1, as well as key findings and next steps for Phase 2. It is structured as follows:
• Sections 3 and 4 summarise the key takeaways from the stocktake exercise.
• Sections 5 and 6 provide the overall conclusion and key findings, as well as the next steps in Phase 2 to advance the discussion on the relevance of transition plans to micro-prudential authorities’ mandate, toolkit, and the overall prudential framework.
3. Overview of current frameworks and literature on transition plans: Similarities and differences

While there is consensus on a general concept of transition plans, an articulation of an organisation’s forward-looking approach to the transition, there is no commonly agreed definition of what a transition plan entails, including its primary aims and purpose, intended audience and precise scope, content and form. This often results in debates on the relevance of transition plans to regulatory objectives being held at cross purposes. This section seeks to set out some of the current frameworks.

Most available frameworks and literature on transition plans are market-oriented, generally applicable to all industries and sectors, and disclosure-focused. Their main objective is to enhance transparency and provide information to shareholders, investors, and other external audiences about an individual corporate’s transition strategy and provide comfort on the credibility of its net zero/transition-related commitments.

There are clear connections between climate transition plan requirements and the Financial Stability Board’s Task Force on Climate-related Financial Disclosures (TCFD) recommendations and, in the future, those of the International Sustainability Standards Board (ISSB), including effective governance, strategic decision-making to manage long-term risks, and metrics and targets to monitor the delivery of the plan.

Transition plans prepared building on these disclosure frameworks could provide useful information to micro-prudential authorities, but they also include elements that may be outside some authorities’ remit (e.g. financing innovation), or information not relevant to addressing climate-related financial risk.

Below are examples of some of these more recent frameworks at the time the NGFS undertook the stocktake. See Annex 1 for the complete list of documents reviewed.

Task Force on Climate-Related Financial Disclosures (TCFD)

The TCFD Guidance⁴ defines a transition plan as “an aspect of an organization’s overall business strategy that lays out a set of targets and actions supporting its transition toward a low-carbon economy, including actions such as reducing its greenhouse gas (GHG) emissions”. Firms’ transition plans are of particular interest to users in understanding how firms will adjust their strategies or business models – including the specific actions they will take to reduce risks and increase opportunities – as they transition to a low-emission economy. In addition, firms’ transition plans should reflect their respective individual circumstances, including relevant industry-specific information.

The guidance describes key characteristics of effective transition plans, elements to consider when developing transition plans (organized by the four pillars of governance, strategy, risk management and metrics and targets), and the types of transition plan information firms should include as part of their disclosure of climate-related financial information. In particular, firms are also encouraged to disclose, inter alia, (i) current GHG emissions performance; (ii) impact on businesses, strategy, and financial planning from a low-carbon transition; and (iii) actions and activities to support transition, including GHG emissions reduction targets and planned changes to businesses and strategy.

¹ TCFD (October 2021) Guidance on Metrics, Targets and Transition Plans.
The ISSB exposure draft, building upon the TCFD recommendations, requires an entity to disclose information about how the entity has responded to, or plans to respond to, climate-related risks and opportunities in its strategy and decision-making including how it plans to achieve any climate-related targets it has set. Similar to the TCFD, the ISSB exposure draft requires disclosure of information to investors about an entity’s plans to respond to climate-related financial risks and opportunities, including climate-related targets, plans to achieve these targets, review processes and qualitative and quantitative information on progress against prior disclosed plans. These, along with the other ISSB disclosures around strategy and decision making, are broadly aligned with the TCFD’s key characteristics and components of effective transition plans.

Compared to TCFD, the ISSB exposure draft, as well as the clarifications made in the most recent deliberations, requires more granular and specific information about current and anticipated changes to business models, including assumptions made and dependencies identified in developing the entity’s transition plans, the entity’s current and planned resourcing for these plans, the entity’s gross emissions targets and intended use of carbon credits in achieving its net emissions targets.

Like the TCFD, the ISSB exposure draft recognises that transition plans have industry-specific nuances. IFRS S2 will require an entity to refer to and consider industry-based metrics that are associated with specific business models, economic activities or other common features that characterise participation in an industry. This may include industry-based metrics associated with an entity’s transition plan.

The SBTi framework for finance, first published in October 2020, provides a target-setting platform and disclosure requirements regarding actions taken by financial institutions to achieve targets. Because financial institutions’ largest emissions impact is through investment and lending activities, the SBTi framework prioritizes target-setting in these areas by adopting an asset class-specific approach. It also contributes to a wider portfolio transition approach than existing frameworks.

The SBTi selected three methods that link financial institutions’ investment and lending portfolios with climate stabilization pathways, each of which can be used for one or more asset classes. The framework includes a headline target that sets out which asset classes are included and how much of the total portfolio is covered, as well as defined targets for individual asset classes that include the method used. Firms must also outline the actions they will take to reach their headline and asset class-specific target(s).

This is in line with the ISSB climate-related standard proposal (see above), that requires an entity to disclose its climate-related targets including, inter alia, transition related elements (e.g., “metrics used to assess progress towards reaching the target and achieving its strategic goals, such as the “transition period/plan element” and “the objective of the target” (e.g., mitigation, adaptation or conformance with sector or science-based initiatives”).

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1 IFRS (March 2022) IFRS S2 Climate-related Disclosures exposure draft.
2 September Staff Paper AP4A: Summary of comments (Question 11), October 2022 ISSB Update, December 2022 ISSB Update.
The Glasgow Financial Alliance for Net Zero (GFANZ)

GFANZ is the world’s largest coalition of financial institutions voluntarily committed to net zero, with its members accounting for 40% of global private finance. In November 2022, GFANZ published a globally-applicable, common, pan-sector framework\(^\text{(1)}\) to support financial institutions in developing credible and comparable transition plans to deliver on their net zero commitments. The Net-Zero Transition Plan (NZTP) framework was developed by a diverse group of financial sector practitioners and informed by an open consultation.

The GFANZ approach emphasizes the importance of financial institutions supporting the whole-economy transition to net zero, rather than reducing financed emissions by simply divesting from emitting companies or assets. The framework provides that a financial institution should perform a review of its “entire business”, with the four key financing strategies that comprise transition finance and provide a lens for understanding whether activities may be aligned with the transition. Financial institutions can support emissions reductions by scaling four key financing strategies by financing or enabling:

(i) Entities and activities that develop and scale climate solutions.

(ii) Entities that are already aligned to a 1.5 degrees C pathway.

(iii) Entities committed to transitioning in line with 1.5 degrees C-aligned pathways.

(iv) The accelerated managed phaseout (e.g., via early retirement) of high-emitting physical assets.

GFANZ defines a transition plan as “a set of goals, actions, and accountability mechanisms to align an organization’s business activities with a pathway to net zero GHG emissions that delivers real-economy emissions reduction in line with achieving global net zero”. It therefore interprets transition plans as a strategic action plan covering an organization’s entire business. For GFANZ members, the framework specifies that “a transition plan should be consistent with achieving net zero by 2050, at the latest, in line with commitments and global efforts to limit warming to 1.5 degrees C, above pre-industrial levels, with low or no overshoot,” as members have each independently committed to achieving net zero in line with the ambition of the Paris Agreement.

The guidance encourages financial institutions to regularly review and update their transition plans in light of the evolution of climate-energy scenarios and the implementation of these plans. While the GFANZ framework does not focus on disclosure, the guidance builds on the TCFD’s recommendations on transition plans and financial institutions are encouraged to disclose relevant components of their transition plans.

The framework builds out the ten key components of a transition plan, which are grouped into five major themes:

(i) **Foundations** – Defining the organization’s overall strategy for reaching net zero, identifying overall objectives and priorities, including interim and longer-term targets and priority transition financing strategies.

(ii) **Implementation strategy** – Translating transition objectives into concrete action across the business in three components: 1. *Products and services* to support and increase client and companies’ efforts to transition; 2. *Activities and decision-making:* embedding net zero priorities into core evaluation and decision-making tools and processes; and 3. *Policies and conditions:* establishing organization-wide policies on priority sectors and activities.

(iii) **Engagement strategy** – Engaging with three key stakeholder groups: 1. *Clients and portfolio companies:* on their own net zero strategies and plans; 2. *Financial industry:* with peers in the sector, as appropriate, to address common challenges and present a cohesive voice; and 3. *Government and public sector:* working to ensure that lobbying and public sector engagement support an orderly net zero transition.
(iv) **Metrics and Targets** – Developing a suite of metrics and targets that reflect both execution of the transition plan and progress over time reflecting real-economy emissions reductions.

(v) **Governance** – Embedding the transition plan in senior levels of governance in the organization and ensuring accountability in two areas:

1. *Roles, responsibility, and remuneration*: clear responsibilities for the board (or equivalent strategic oversight body) and senior management, with remuneration incentives used where possible; and
2. *Skills and culture*: Provide necessary training and embed the transition plan into the institution’s culture and practices.

The GFANZ net zero transition plan framework can be used by any financial institution globally to develop a transition plan. The UK’s Transition Plan Taskforce has published a transition plan disclosure framework for UK companies and financial institutions, which builds on and is aligned with the GFANZ global framework.

One theme that arose over the course of the stocktake but was outside of the scope of the literature review and survey, was the importance of “credibility” in transition plans. Specifically, the NGFS discussed the importance of understanding how credibility of a transition plan is determined or defined, and who is best placed to assess it.

**Why is it important to have credible transition plans and how is it defined?**

Credible transition plans can communicate the actions a corporate intends to take to achieve its transition strategy. For financial regulators, it can minimise the risk of greenwashing, including enabling micro-prudential authorities to place reliance on the information and the implications for the financial risks that a financial institution faces.

Several of the transition plan frameworks described above set out an expectation for transition plans to be ‘credible’. These frameworks that seek to define ‘credibility’ do so from the perspective of climate risk materiality to the institution and its net zero objective. These may not necessarily align to national plans and pathways which may also need to be considered.

At a high level, the main features of a credible net zero transition plan would include:

- A scientifically aligned, long-term goal to significantly mitigate the worst impacts of climate change, supported by a credible trajectory (such as a Paris-aligned goal of net zero by no later than 2050). For financial institutions, the most material part will deal with the allocation of capital that is aligned to a net zero pathway, not only through the direct use of its balance sheet, but also through wider activities such as organising finance, portfolio alignment targets, transition financing targets and sector-based financing policies with time-bound exclusions and action plans.
- A clear approach to align business activities to the stated target that should drive in GHG emissions reductions.
- Robust governance, accountability and remuneration frameworks for the delivery of the plan, incorporating both short and long-term deliverables and milestones.
- The application of an “emissions budget” which sets an absolute cap on total emissions over the life of the transition plan. Emissions exceeding the planned trajectory in any given period must be deducted from the budget. To stay below the budget cap, the planned emissions trajectory must therefore accelerate. (And vice-versa for any period where emissions fell below the planned trajectory.)
- Shorter term, achievable milestones that are aligned to progressive fulfilment of long-term net zero goals which provide check points for the plan and enables refinements and modifications in light of updated data and scientific methods emerging over time.
- Measurable and verifiable deliverables and engagement strategy primarily focused on supporting the reduction of real-world emissions. Metrics that adequately capture all material sources of emissions and disclosed in a meaningful way to stakeholders.
- Transparency of the risks, challenges, dependencies, and assumptions for implementation – such as technological barriers, political risks, business risks, and shareholder pressures – and possible mitigants to these hurdles.
- Assessment of how influencing initiatives are consistent with a net zero goal, particularly for activities that are highly vulnerable to the perception of “greenwashing” such as political contributions, government lobbying, research activities, marketing, education, disclosures, and response to shareholder proposals.

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1 The use of carbon credits or offsets should also be duly considered. This should not count towards the emission reduction targets, which should be done by reducing actual emissions. But offsets and carbon credits should be nonetheless disclosed and substantiated. For example, the UNEP Guidelines for Climate Target Setting for Banks state: “The reliance on carbon offsetting for achieving end-state net-zero should be restricted to carbon removals to balance residual emissions where there are limited technologically or financially viable alternatives to eliminate emissions. Offsets should always be additional and certified.” The intended use of carbon credits also needs to be disclosed under the ISSB exposure draft, as well as in the EU ESRS (which importantly does not allow the use of offsets in the emission reduction targets).
The G20 Sustainable Finance Working Group recently provided recommendations to enhance transition plan credibility. This included the recommendation to use independent third-party verification/assurance to verify the information in transition plans. Further guidance is also proposed in the ISSB’s Exposure Draft for Climate-related Disclosures (para 13) on transition plan disclosures. This enables stakeholders to understand the effects of climate-related financial risks and opportunities on an entity’s strategy and decision-making, including information on how it plans to achieve any climate-related targets and measures of the progress of plans.

Who is best placed to assess the credibility of transition plans?

The above definition of credibility creates a high threshold for assessing transition plans credibility from a scientific perspective. At present, micro-prudential authorities do not have the appropriate resources or skills to make these assessments and provide the rigorous challenge required. Being tasked with this assessment would require significant capacity building. Furthermore, the above definition is founded on the need to minimise greenwashing risks, which can be outside some micro-prudential authorities’ remit.

In terms of resources or skills, there may be other actors who could prove better placed to assess the credibility of transition plans of financial and non-financial firms at a lower cost, and whose assessments can then be used by micro-prudential authorities. This could include public or private actors, such as certain ministries or public authorities in each jurisdiction, or private actors such as verifiers, including but not limited to auditors, consultants, or specialist climate advisory firms.

Regardless of whether public or private actors should be engaged to independently assess the credibility of transition plans, it is likely that this approach would enable a broader cohort of transition plans to be independently verified and adequately monitored than if relying on supervisory resources alone. In particular, it could facilitate a more thorough assessment of how credible financial and non-financial firms’ transition plans are from a scientific perspective and whether their ambitions and targets are appropriately aligned to the pathway in question.

Given that independent third-party verification of transition plans would feed into the usability of these plans for micro-prudential authorities, it is essential that any verification process is both robust and any such services would need to scale to meet the demand of financial and non-financial firms developing transition plans.

This point on verifying credibility has arisen in the course of the Phase 1 stocktake, which indicates the need for further exploration.

2 Exposure Draft IFRS S2 Climate-related Disclosures.
4. Overview of the current state of play in different jurisdictions

While the development and disclosure of transition plans within the regulatory and legislative domain is relatively nascent, below are a summary of NGFS members’ approaches and views on transition plans, as well as examples of some approaches that regulators and governments are undertaking.

4.1. Current state of play among NGFS members

The NGFS undertook a survey of NGFS members in 2022 on the member jurisdiction’s as well as their institutional approaches to transition plans with a view to understanding the actions members have taken to date, and to develop over time the connection between transition plans and the responsibilities, objectives, and mandates of micro-prudential authorities of both the banking and the insurance sectors. In total, the NGFS received 48 responses.

Overall, respondents are still developing their views and approaches towards transition plans, the contents of these plans, and the role of micro-prudential authorities in mandating or using them.

The majority of respondents indicated that the role of micro-prudential authorities in relation to transition plans has not been defined/agreed/communicated in their jurisdictions. This includes authorities in both less and more advanced markets. Only a small minority of NGFS members have mandated transition plans (three members out of 48) or have established a definition of what a transition plan should be, entails or covers.

**There is no commonly agreed definition of transition plans across respondents.** Some jurisdictions base their definitions on jurisdiction-specific climate commitments, while others signalled an intent to align with internationally accepted frameworks, such as the TCFD. Broadly speaking, respondent definitions could be grouped into those focusing on (i) reducing GHG emissions and (ii) reducing exposure to climate-related risks (with emissions reduction as a potential secondary goal).

Further, a large part of respondents indicated that they see transition plans as having a role to play in mitigating risk, but many of them have yet to firm up their thinking in this area.

(All percentages referenced in this section are from a total of 48 respondents)

- Majority (52%) of respondents see transition plans as having a role to play in mitigating risk.
- However, many (40%) of the respondents have yet to firm up their thinking in this area.

While acknowledging that risk management could be an objective of transition plans, respondents have not, in general, articulated if, and what, should be the role of micro-prudential authorities in mandating or using transition plans.
About two thirds (69%) of respondents have yet to decide on the role of micro-prudential authorities.

Of the remaining, most (14 of 15) are considering transition plans in the context of risk management tools for institutions, with some mentioning the need to consider supporting global decarbonisation efforts (and an orderly transition). Notwithstanding, NGFS members foresee the possibility of using these plans as tools or data points, to: (i) understand the transition strategy of supervised financial institutions, (ii) monitor firm’s progress in addressing climate-related financial risks (e.g., the change in a firm’s business over time and associated risk management) and to (iii) manage these risks at a sector-level (e.g., financial stability).

As a result, many respondents were still firming up their approaches towards transition plans.

A little more than half of the respondents have considered transition plans as either a combination of risk management and strategy/climate policy tool or a risk management tool for financial institutions.

The remaining respondents (48%) have yet to decide on how to approach transition plans.

Respondents also acknowledge that transition plans could have purposes beyond managing risk, such as being a source of information, and to facilitate alignment with broader national climate policy objectives.

The divergence in approaches and the ways in which micro-prudential authorities engage with transition plans appears driven, in part, by the mandates, and the existence, or not, of jurisdiction-specific legislation and requirements to ensure alignment with specific climate outcomes beyond just safety and soundness (e.g., definition of transition plans, requirements for transition plans, whether and how the credibility of those plans is assessed).

While acknowledging that financial institutions are expected to mitigate risks arising from climate change, most (79%) respondents have not identified transition plans as mandatory tools to do so. When discussing the components of a transition plan, a small majority of the surveyed respondents have either not determined the value of transition plans or do not believe transition plans will provide essential information or value above and beyond

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5 57% of respondents do not have determined a transition plan framework yet, 21% are currently building it or planning to do so, and 23% have binding or non-binding framework in place.
what a micro-prudential authority would obtain from firms embedding existing principles/guidance on management of climate related financial risk. The remaining surveyed respondents indicated that the transition plan provides essential information or value to the prudential authority above and beyond what authorities would obtain from firms embedding existing principles/guidance on management of climate-related risks (e.g., NGFS or BCBS principles).

**Most respondents have yet to determine the relevant regulator/supervisor of transition plans.** At the current juncture, the information included in financial institutions’ transition plans is seen as potentially serving different regulatory/supervisory objectives, such as safety and soundness, financial stability, market conduct/integrity (including concerns over greenwashing) and/or to deliver on specific climate outcomes such as meeting Paris Agreement targets). These objectives are non-exclusive.

Notwithstanding the uncertainty around the role of regulators and supervisors in relation to transition plans, some respondents have started discussions with financial institutions on transition plans.

**Chart 4 Engaging FIs around transition plans**

- Some (42%) of respondents have already started or plan to engage with supervised institutions regarding transition plans.
- Of those that have, this was often done in the context of ongoing supervisory dialogue, as well as for fact-finding and capacity building purposes.

NGFS members identified the need for different authorities/audiences (both public – relevant ministries / financial regulators / development banks / government agencies / state owned energy companies – and private – business associations in relevant sectors, industry, scientific bodies, think tanks) to be involved and coordinate actions, for example through the establishment of Joint Committees or Action Plans. This type of approach should contribute to improve: (i) the understanding of what constitutes a credible transition plan, (ii) the availability of data and standardized metrics and definitions in the area of disclosures, through a collaboration with financial reporting authorities, and (iii) harmonize the consistency of supervisory approaches and reduce overlaps across authorities.

## 4.2. Examples of jurisdictional approaches to transition plans

In some jurisdictions, regulators have specific mandates on climate-related risks, whilst other jurisdictions have an indirect mandate via their support to government policies, or no specific mandate on climate change. According to a study by the LSE Grantham Institute on central bank mandates, sustainability objectives and the promotion of green finance found that out of 135 central banks, 12% have explicit sustainability mandates, while 40% are mandated to support the government’s policy priorities, which mostly include sustainability goals⁶. The study also found that the inclusion of a direct or indirect sustainability mandate did not strongly correlate with the choice of policy framework. The study found that many central banks that did not have a sustainability mandate had nevertheless begun to address climate change risks in so far as they relate to their core objectives.

The following section provides an overview of some examples of jurisdictional approaches to transition plans.

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⁶ Central bank mandates, sustainability objectives and the promotion of green finance – Grantham Research Institute on climate change and the environment (lse.ac.uk)
The European Union (EU) approach

The EU's 2020 European Green Deal introduced a package of policy initiatives which support the policy objective for institutions to align their business strategies with the EU's jurisdiction-specific climate outcome. At the date of writing there are also a number of (passed and ongoing) legislative initiatives to require financial and non-financial corporations to develop and publish climate transition plans in the EU.

First, with regard to both financial and non-financial corporates, Article 19a of the Corporate Sustainability Reporting Directive (CSRD) (adopted and published on 14 December 2022 and coming gradually into effect 2025-2028) stipulates that firms in its scope are required to disclose plans to ensure that their business model and strategy are compatible with the transition to a sustainable economy and with the limiting of global warming to 1.5 °C in line with the Paris Agreement and the objective of achieving climate neutrality by 2050 as established in the European Climate Law, and, where relevant, the exposure of the undertaking to coal-, oil- and gas-related activities. They are also required to disclose a description of their time-bound targets related to sustainability matters, including, where appropriate, absolute GHG emissions reduction targets at least for 2030 and 2050, a description of the progress the undertaking has made towards achieving those targets and a statement of whether its targets related to environmental factors are based on conclusive scientific evidence.

The CSRD is supplemented by European Sustainability Reporting Standards (ESRS) developed by the European Financial Reporting Advisory Group (EFRAG) and due to be adopted by the European Commission as delegated acts. The draft ESRS contain very explicit and standardised requirements on transition plans for climate change mitigation. These requirements include that, when disclosing, companies may consider the cumulative locked-in GHG emissions associated with key assets in tCO2eq, the cumulative locked-in GHG emissions associated with the direct use-phase GHG emissions of sold products in tCO2eq, and an explanation of the plans to manage, i.e., to transform, decommission or phase out its GHG-intensive and energy-intensive assets and products. They should also provide an explanation of how the transition plan is embedded in and aligned with the undertaking's overall business strategy and financial planning.

Second, the Commission's proposal on the Due diligence Directive, still being negotiated at the time of drafting, contains a draft article 15 (combating climate change) which would make transition plans mandatory by requiring large companies (credit institutions included) to adopt a plan to ensure that their business model and strategy are compatible with the transition to a sustainable economy and with the limiting of global warming to 1.5 °C in line with the Paris Agreement.

Third, with regard to banking institutions specifically, the EU Commission's proposal for the new banking package (EU Capital Requirement Regulation (CRR3) and Capital Requirement Directive (CRD6)), still being negotiated at time of drafting, requires banks to have in place specific plans and quantifiable targets to monitor and address the risks arising in the short, medium and long term in the transition to a more sustainable economy. It also…


2. The CSRD applies to all EU large companies (exceeding two of the following criteria: (a) balance sheet total: EUR 20 000 000; (b) net turnover: EUR 40 000 000; (c) average number of employees: 250) and all companies listed on EU regulated markets except listed micro undertakings. For non-European companies, the requirement to provide a sustainability report applies to all companies generating a net turnover of EUR 150 million in the EU and which have at least one subsidiary or branch in the EU exceeding certain thresholds.

3. See EFRAG, First Set of draft ERS.

4. [Draft] ESR E1 Climate change.


6. The current proposed wording of the CRD (recital 34 and 76(2)) by the Council includes: “[…] specific plans, quantifiable targets and processes to monitor and address the financial risks […] from ESG factors, including those arising from the process of adjustment and transition trends towards the relevant Member States and Union legal and regulatory objectives […] in particular those set out in Regulation (EU) 2021/1119 (“European Climate Law”), as well as, where relevant, third country legal and regulatory objectives. […]”. The wording proposed by the Parliament is slightly different, and further revisions are possible during ongoing legislative discussions.
mandates the EBA to set out the minimum requirements and expected content of these transition plans with expectations for competent authorities to monitor and assess them. In this respect, transition plans are expected to be used as a micro-prudential risk management tool.

While there is not yet a commonly agreed definition (due to on-going legislative process) on these prudential transition plans, discussions have nevertheless started at the banking supervision level, as it is expected that banking supervisors (Single Supervisory Mechanism (SSM) for significant Eurozone institutions, National Competent Authorities for other institutions) will be the relevant supervisor for transition plans of financial institutions under CRD; while under CSRD this may be the designated national competent authority as identified in national law transposing this Directive (usually the securities / market authority).

Reflections are on-going on the content of risk-based transition plans, be it at the EBA or SSM levels, taking a micro-prudential approach as per their mandates. Transition plans should provide an overview and articulation of the risk management and strategic actions and tools developed by institutions to ensure their safety and soundness in the process of the transition to a sustainable economy. In particular, they should ensure that institutions identify, measure, monitor, and manage climate-related and environmental risks over longer time horizons than usually considered, taking into consideration the EU policy objectives and legal framework.

The Philippines approach

The Philippines have mandated transition plans for banks. Circular No. 1085, the Sustainable Finance Framework issued in 2020 requires banks, amongst other requirements, to adopt a transition plan with specific timelines to implement the board-approved strategies and policies integrating sustainability principles into their corporate governance and risk management frameworks as well as in their strategic objectives and operations. Banks were given a period of three years from May 2020 within which to comply with Circular No. 1085.

As such, these transition plans are assessed by banks’ micro-prudential authority, the Bangko Sentral ng Pilipinas (BSP), which engages with banks through offsite supervision or onsite examination on discussions of banks’ broad plans and strategies in order to comply with Circular No. 1085.

The BSP does not provide guidelines or a prescribed format with respect to the development and presentation of transition plans. Best practices will be identified based on BSP’s assessment of transition plans, which may feed into potential enhancements in sustainable finance-related regulations issued by the BSP. The BSP will also consider analyses and guidance from external bodies and international organizations for reference.

The assessment of transition plans will be integrated in the BSP Supervisory Assessment Framework. Whether the BSP will hold banks accountable for failure to deliver the plan is still under consideration. More weight, however, is given on the outcome of the review of transition plans submitted by banks for identification of possible best practices, as well as on the current state of awareness and capacity of banks in relation to climate, environmental and social risks management.

Given the Philippines’ climate and sustainability goals (including a GHG emissions cut by 75% in 2030), the BSP expects banks to revisit their strategies, targets, and risk profile and effectively manage their environmental and social risk exposures while contributing to the achievement of such goals.

Meanwhile, the BSP notes that banks are in varied stages of maturity in terms of adopting the Sustainable Finance Framework. There are banks that are considered advanced which have substantially met the provisions of Circular No. 1085 and have likewise adhered to global sustainability and impact reporting requirements, and issued green, social or sustainability bonds.
The UK approach

In the United Kingdom, regulations made under the UK Companies Act require over 1,300 of the largest UK-registered companies and financial institutions to disclose climate-related financial information on a mandatory basis – in line with TCFD Recommendations, to help support investment decisions as the UK moves towards a low-emission economy.

The UK securities and conduct regulator, the Financial Conduct Authority (FCA), explicitly references the TCFD’s guidance on Metrics, Targets and Transition Plans in its TCFD-aligned disclosure rules for listed companies (PS21/23), asset managers and FCA-regulated asset owners (PS21/24). In accordance with its statutory objectives, the FCA recognises that transition plan disclosures support the provision of material forward-looking information to the market and enable listed companies and regulated firms to be held to account for the climate-related claims and commitments that they make.

Encouraging disclosure of transition plans contributes to the FCA’s wider strategic aim to improve transparency of climate change (and wider sustainability) along the value chain. As the FCA notes in its ESG Strategy, “a market led transition to a more stable and less carbon-intensive economy – and a more sustainable future – will require high quality, consistent and comparable information on how climate-related, and wider ESG-related risks, opportunities and impacts are being managed across the economy and the financial sector”. Accompanying guidance to the disclosure rule clarifies that the FCA encourages listed companies, asset managers or asset owners headquartered in, or operating in, a country that has made a commitment to a net zero economy to consider the extent to which it has considered that commitment in developing and disclosing its transition plan.

HM Treasury (HMT) established the Transition Plan Taskforce (TPT) to “establish best practice for firm-level transition plans and develop guidance and a set of templates setting out both generic and sector-specific disclosures and metrics.” In the draft TPT Disclosure Framework, published in November 2022, the TPT defines a transition plan as being “integral to an entity’s overall strategy, setting out its plan to contribute to and prepare for a rapid global transition towards a low GHG-emissions economy”. Under the draft Framework, a corporate transition plan could cover: (i) a firm’s high-level ambitions to mitigate, manage and respond to climate change and to leverage opportunities of the transition; (ii) actionable short and medium-term steps the firm plans to take to achieve its strategic ambition with details on how these will be financed; and (iii) governance and accountability mechanisms that support delivery of the plan with robust periodic information. As part of this, firms might also address material risks and opportunities relating to the natural environment, workforce, supply-chains, communities, and customers that arise as part of their transition plan actions.

The TPT is working to ensure alignment between its framework and the TCFD’s recommendations, the ISSB’s draft standards and the GFANZ framework to ensure international compatibility as far as possible. For example, the framework is designed to integrate with the elements of the ISSB standards and replicates the five pillars in the GFANZ framework (see below diagram).
The FCA has worked closely with the TPT and has committed to drawing on the TPT’s outputs to strengthen disclosure requirements in this area for listed companies and regulated firms. In a Primary Market Bulletin article (PMB 42) published in December 2022, the FCA encouraged listed companies to engage early with the TPT’s draft outputs. Noting that the TPT’s draft Framework builds from and is integrated with the TCFD’s recommendations, the article encourages companies to consider the draft Framework when making their transition plan disclosures in accordance with the FCA’s rules and guidance. In the FCA’s role as conduct regulator, the governance of firms’ transition plans will be relevant – including in relation to Board oversight, senior management responsibilities and objectives and remuneration and incentives arrangements.

While the UK Government legislated in 2019 to commit to net zero emissions by 2050, firm-level net zero commitments are not mandatory. However, the UK TPT does recommend that entities’ transition plans should be informed by national commitments and the latest international agreement on climate change. In line with FCA expectations, UK entities’ corporate transition plans should detail how they will take into account the UK’s legal commitment to net zero by 2050.

The Prudential Regulation Authority (PRA) – the micro-prudential authority – is still considering the role of transition plans in its supervisory practices while simultaneously supporting the work of the TPT. In 2019 the PRA set supervisory expectations, in which the “PRA expects a firm’s board to understand and assess the financial risks from climate change that affect the firm, and to be able to address and oversee these risks within the firm’s overall business strategy and risk appetite. The approach should demonstrate an understanding of the distinctive elements of the financial risks from climate change and a sufficiently long-term view of the financial risks that can arise beyond standard business planning horizons.” Consistent with the UK Government’s approach, the PRA does not set climate targets or require firms to have climate objectives, but it does, in accordance with the PRA’s objectives, have a mandate to assess the climate related financial risks to which firms are exposed as a result of the firm’s strategy and risk appetite, including in relation to the risks of transition and aspects of any corporate transition plan identified by the firms themselves. Transition plans could, if relevant, feed into the PRA’s assessment of progress against the expectations in Supervisory Statement SS3/19.
The FCA will assess the first set of TCFD disclosures in relation to its initial expectation as part of its wider supervision of climate-related disclosures and expects to consult on its disclosure expectations for transition plans once the TPT framework has been finalised. In its role as conduct regulator, the FCA will have an important role in assessing the governance surrounding transition plans disclosed by regulated firms, including in relation to Board oversight, senior management responsibilities and objectives and remuneration and incentives arrangements.

The US approach

In the US, firms are not required to develop transition plans, nor are supervised institutions required to align to US climate targets or set their own targets. From a supervisory perspective, the US banking agencies expect firms to demonstrate robust management of all material risks, including those related to climate change. If supervised firms issue transition plans on a voluntary basis, supervisors may have an interest in the governance and risk management components of the plan for the purpose of assessing risks to the institution’s safety and soundness.

Unlike some supervisory authorities in other jurisdictions, US banking agencies (the Federal Reserve Board (FRB), the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation) do not have a mandate to promote or facilitate a transition to a low carbon economy. The US banking agencies are responsible for ensuring the safety and soundness of individual financial institutions and promoting the stability of the financial system more broadly.

From a disclosure perspective, US firms are not required to disclose transition plans. At the time of writing, a draft pending rule from the Securities and Exchange Commission (SEC) proposes that a public firm disclose its transition plan if it was voluntarily adopted as part of the firm’s climate-related risk management strategy.

Micro-prudential authorities’ approach to climate risk management is guided by international standard setting bodies (SSBs), including the Basel Committee on Banking Supervision (BCBS) and the International Association of Insurance Supervisors (IAIS). Whilst these SSBs have developed supervisory guidance around climate risk management, they currently do not explicitly capture the micro-prudential authority’s role regarding transition plans. Instead, the Basel Core Principles (BCPs) and Insurance Core Principles (ICPs) establish that an institution should develop and implement a sound process for understanding and assessing the potential impacts of climate-related risk drivers on its businesses and on the environments in which it operates.

• BCBS: In addition, in June 2022 the BCBS published *Principles for the effective management and supervision of climate-related financial risks*. These 18 high-level principles provide guidance to both banks and prudential supervisors. They are intended to foster global alignment through the development of a common baseline, while maintaining flexibility given the heterogeneity and evolving practices in this area. The BCBS review of the existing Basel framework concluded that the BCPs and supervisory review process were sufficiently broad and flexible to accommodate additional supervisory responses to climate-related financial risks. The principles and FAQs published in December 2022, provide a foundation for the regulation, supervision, governance and risk management of climate-related financial risks.
• **IAIS**: The IAIS work focuses on promoting a globally consistent supervisory response to climate change, and providing supervisors with the necessary tools to monitor, assess and address climate-related financial risks to the insurance sector. To support this, in May 2021 IAIS published the *Application Paper on the Supervision of Climate-related Risks in the Insurance Sector*. The IAIS is closely monitoring developments in global climate change mitigation efforts, climate science and how supervisory practices to manage climate-related risks have evolved. As a result of that, the IAIS has identified possible further work in terms of standard-setting and providing further guidance on supervisory practices and intends to publicly consult on limited changes to guidance related to various ICPs and to develop supporting material in several consultations over the next 18 months. The first consultation was published in March 2023.
Based on the work undertaken, there are a range of current frameworks regarding transition plans, which predominantly relate to climate-related corporate disclosures applicable to both financial and non-financial firms. The utility of these frameworks and literature is limited by the variety of lenses through which they are defined, which generally go beyond the micro-prudential authorities’ remit and may not entirely or precisely meet their needs. See key findings 1, 2 and 3 below.

Furthermore, there is interest among NGFS members to understand how transition plans may be relevant to micro-prudential authorities’ regulatory objectives. However, there are differing perspectives on the role of the micro-prudential authority in requiring transition plans, as regulators grapple with their unique jurisdictional approaches to addressing climate change, regulatory mandates, and financial system regulatory infrastructures. While micro-prudential authorities can conceptually see uses for the information contained in transition plans to assess and monitor risk, there are differing perspectives on whether micro-prudential authorities (versus others, such as the government) should mandate transition plans. Furthermore, if micro-prudential authorities mandated these plans, there were differing perspectives on what they would assess.

The stocktake suggests a common foundational need of micro-prudential authorities to have information that enables them to develop a forward-looking assessment of financial institutions. This could include a view on an institution’s strategy toward the transition to a low emission economy or to meet certain climate targets (where transition goals of the firm might be voluntarily adopted or mandated by governments), understand the risk profile of an institution, and whether the risks are commensurate with its risk management framework. To name a few examples, micro-prudential authorities could be keen to understand how financial institutions adjust their financing decisions over time as the economy changes, how financial institutions engage with the counterparties to keep them in line with sectoral trajectories, whether it will set aside more capital to deal with the growing transition risks from laggard counterparties, etc.

A transition plan is not necessarily the only means to obtain such information, but the stocktake suggests micro-prudential authorities may at a minimum be users, alongside other stakeholders, of transition plans for the purpose of addressing climate-related risks. However, in some instances reflecting specific national circumstances, authorities may also play a greater role, such as being a standard setter and supervisor of transition plans. Therefore, any guidance to micro-prudential authorities should be flexible and consider a building block approach to recognize the spectrum of regulatory objectives. See key findings 3, 4, and 5 below.

Lastly, the role that micro-prudential authorities play needs to be situated in the context of the actions of other financial and non-financial regulators and to avoid duplicate or inconsistent requirements being imposed on institutions. Climate change is a global issue that needs to be addressed by financial and non-financial firms alike with potentially cross-jurisdictional implications. See key finding 6 below.

**Key finding 1: There are multiple definitions of transition plans, reflecting their use for different purposes**

Our findings above show that there are multiple definitions of transition plans, reflecting their use for different purposes. A few different frameworks exist which view transition plans through different lenses. Similarly, jurisdictions who developed expectations around transition plans have done so based on their unique circumstances, and many are still in the process of firming up of their approach.

**Table 1** summarises the different types of transition plan use cases, including the nuances in their scope and purpose. The stylised transition plan use cases, while non-exhaustive, aim to capture, at a high level, the potential orientation of these plans depending on jurisdictional requirements or expectations (notwithstanding the potential for overlapping or integrated use cases). Based on these use cases for transition plans, we conclude that transition plans can broadly be categorised into:
a) **Strategy-focused transition plans**, which are broad in scope in content and application (e.g., financial and non-financial firms). They are primarily intended to provide transparency to external audiences, including shareholders and investors, on a firm’s strategic approach to meet specific climate commitments or targets (e.g., Paris-aligned, government policy, or firm-defined voluntary target), such as actions and targets to support the transition to net zero through and the resultant impact on, or and preservation of, the firm’s enterprise value.

While primarily directed toward shareholders and investors, these plans could serve the needs of a broad range of audiences including financial regulators such as micro-prudential authorities, market conduct regulators, and authorities responsible for financial stability. Given their purpose, these types of plans are more likely to be publicly disclosed and publicly available.

One example of this type of plans is the GFANZ framework7. As highlighted in Section 3, one of the key themes GFANZ focuses on is the engagement strategy, including engagement with the government and public sector to lobby and engage the public sector in support of an orderly net zero transition.

Furthermore, as highlighted in Section 4.2, the EU, through legislation, stipulates that financial and non-financial firms are required to disclose transition plans, when applicable, to ensure that their business model and strategy are compatible with the transition to a sustainable economy and with the EU’s 2030 and 2050 climate-related targets. The UK TPT framework is another example of this type of transition plan.

b) **Risk-focused transition plans**, which are narrower in scope in content and application (e.g., financial institutions) than strategy-focused plans. These plans are primarily focused on how institutions will manage the financial risks associated with the transition to a low emission economy. Given these are more internal/regulator-facing documents, the decision as to whether to publicly disclose these transition plans will depend on decisions by the institution, or by the respective regulator.

One example, as highlighted in Section 4.2, is the Philippines, where the micro-prudential authority has mandated transition plans for banks where, amongst other requirements, they have to adopt a transition plan with specific timelines to implement the board-approved strategies and policies integrating sustainability principles into their corporate governance and risk management frameworks as well as in their strategic objectives and operations.

Table 1 also highlights a key challenge that financial institutions could face when developing transition plans, as these plans may need to address the needs of multiple audiences, including different financial regulators. Financial institutions and regulators alike need to consider the practicalities (i.e., synergies and complexities) of having different plans for different objectives versus an integrated plan that meets multiple objectives and ensures consistency of the information.

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Key finding 2: There is merit in distinguishing transition planning (transition strategy) from a transition plan (transparency to a specific audience)

Another key finding from the stocktake is the different ways to interpret what might be entailed in the process of ‘transition planning’ versus a ‘transition plan’.

For the purposes of this stocktake, we distinguished a) ‘transition planning’ from b) a ‘transition plan’ in the following way, drawing a line between what is an internal process and what is an external-facing product:

a) Transition planning is the internal process undertaken by a firm to develop a transition strategy to i) deliver climate targets that firms may voluntarily adopt or that are mandated by legislation or the appropriate authority, and/or ii) prepare a long-term response to manage the risks associated with a transition to a low emission economy.

The steps taken in this internal planning process might include, for example, assessing relevant physical, operational, business and counterparty transition risks, designing the appropriate frameworks and management processes and approving any final strategic decision-making through the necessary internal governance channels.

Transition planning may also have implications for the institution’s risk profile and exposure to financial risks. To implement the actions from the planning process, institutions may need to make changes to their governance, risk management practices, board engagement as well as directly to the strategy itself. These changes could include:8

- Gaining board and senior management buy-in, including learning and review cycles to keep the plan under continuous review and allowing the firm to incorporate emerging opportunities and updated scientific insights

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Table 1 Categories of transition plan use cases

<table>
<thead>
<tr>
<th>Actor requiring transition plans</th>
<th>Government</th>
<th>Corporate</th>
<th>Financial Regulator</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulatory objective</td>
<td>Climate outcomes (e.g., Paris Agreement)</td>
<td>N/A</td>
<td>Market conduct / consumer protection</td>
</tr>
<tr>
<td>What is the primary objective of the transition plan?</td>
<td>Achieve national climate outcomes through corporate action</td>
<td>Inform shareholders and investors of a corporate’s strategy in response to climate change and transition</td>
<td>Provide transparency to market actors e.g., maintain market integrity, prevent financial misconduct and/or greenwashing</td>
</tr>
<tr>
<td>What is the primary tool to achieve that purpose?</td>
<td>Disclosure of strategy to meet climate targets</td>
<td>Disclosure of strategy to meet climate targets</td>
<td>Disclosure of strategy to meet climate targets</td>
</tr>
<tr>
<td>Who is the primary audience?</td>
<td>Public</td>
<td>Shareholders and investors</td>
<td>Market participants, consumers</td>
</tr>
<tr>
<td>Is the information publicly available?</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>

8 Climate Safe Lending Network/UN PRI (2021): The Good Transition Plan.
• Embedding the transition plan into the core strategy to update the regular strategy processes and ensuring new climate elements in the core strategy are kept up to date in line with e.g., business model, demand-related, technological, scientific or sectoral evolutions.
• Integrating transition planning in its risk management framework and corresponding risk processes and practices.
• Measuring how much carbon and other GHG the firm is financing, and monitoring improvements
• Setting targets for reducing financed carbon and other GHG emissions, using science-based targets and credible climate change scenarios

b) Transition plans are a key product of the transition planning process and are an external-facing output for external audiences, such as investors and shareholders and regulators. They provide transparency on the strategy of how a corporate plans to align their core business with a specific strategic climate outcome, addressing, amongst other things, the business changes required for transition, assumptions, dependencies and sensitivity analysis associated with the transition strategy, implication of the chosen strategy on institution risk profile and risk management practices, and the resulting impact on enterprise value. Transition plans are, therefore, a useful tool which bring together various aspects of the transition planning process for external audiences.

Whether transition planning processes are articulated through a formal ‘transition plan’ document that is publicly disclosed is a decision that may be made by different stakeholders at different levels: voluntarily by an individual financial institution itself, mandated by regulators within individual jurisdictions, or by government to comply with broader government policy.

While the transition planning process may not result in a transition plan document, articulating such planning into a formal transition plan, used also for disclosure purposes, may bring additional benefits – for example helping the financial system to efficiently allocate capital toward transitioning to a low emission economy – as well as potential additional risks, such as reputational and litigation risks. For transition plans to be a useful tool to the spectrum of users, they would benefit from stronger coordination and standardisation by the different authorities.

Key finding 3: Existing frameworks speak to a mix of objectives, audiences and concerns for transition plans but predominantly relate to climate-related corporate disclosures

A key challenge the NGFS encountered was navigating the variety of frameworks and literature to identify elements that could be useful to micro-prudential authorities and distilling views to find common ground. While the central concept of strategy-focused plans may be well understood – an articulation of an institution’s approach to achieve its transition strategy – the available frameworks and literature speak to a mix of objectives, audiences, and concerns.

The literature and available frameworks predominantly relate to climate-related corporate disclosures applicable to both financial and non-financial firms. A few frameworks envisage a specific role for financial regulators. Where the literature and frameworks do advance a specific role for regulators, there is no consistency on which regulatory objectives are being advanced, ranging from managing climate-related risks, which may speak to the micro-prudential regulators’ role, to financial stability, which may speak to macro-prudential regulators, to market integrity and conduct, which speaks to securities regulators.

As stated above, transition plans prepared using current available frameworks and literature are primarily focused on corporate strategy or whose primary objective is to assess the potential impact on enterprise value to stakeholders. They are intended to be used by a broader audience than those which are primarily focused on the financial risk-management aspects of transition. As a result, these plans are likely to be broader in scope and may have elements that are beyond the interests and remit of a micro-prudential authority.

If financial institutions produce strategy-focused transition plans either voluntarily or as mandated by government or regulators with the relevant mandate to do so, the information needs of the micro-prudential authority may be met by, for example, using transition plans disclosed as part of these disclosures (i.e., rather than requesting a separate plan).

However, it is unlikely that micro-prudential authorities would be able to set the expectations based on transition
plans that take a broader, strategic approach given micro-prudential authorities’ narrower remit focused primarily on safety and soundness. Therefore, how transition plans are defined, i.e. to encompass strategic perspective, the risk perspective or to provide both, can impact supervisory expectations and determine the most appropriate and optimal use of these plans by regulatory authorities in respect of their objectives.

Key finding 4: Transition plans could be a useful source of information for micro-prudential authorities to develop a forward-looking view of whether the risks resulting from an institution’s transition strategy are commensurate with its risk management framework

The role of micro-prudential authorities – as well as other financial regulators responsible for financial stability, market conduct and integrity – in addressing climate change will be dependent on the national institutional framework for financial regulation as well as the national framework for addressing climate change across the whole economy. That will likely lead to differing approaches in jurisdictions to achieve international commitments.

Micro-prudential authorities seek to understand a financial institution’s strategy to respond to/prepare for the risks associated with climate change. Hence, transition plans could be important to understanding the financial risks the institution is exposed to as a result of its strategy, its risk appetite, and whether it has effective risk management in relation to its climate-related risks.

Transition plans can support risk management and business strategies. They can help financial institutions and micro-prudential authorities overcome some conceptual challenges with climate-related risks, including, for example, limited data availability,9 challenges with different time horizons,10 and the backward-looking nature of current methodologies.11 Against that background, transition plans can be used as a proxy for long-term risks.12

In addition, micro-prudential authorities can use them not only to monitor but help supervise financial institutions’ short- and long-term strategy to manage climate-related risks and understand how different transition pathways can affect an institution’s safety and soundness. Transition plans can help authorities to understand the institutions’ approach to the management of climate-related (transition) risks – notably by being bound with stress tests, internal capital adequacy assessment process (ICAAPs), etc., thereby extending a short-medium-term perspective of risk management tools.

While the micro-prudential authority is focused on how institutions’ strategies and management of climate-related risks could affect their safety and soundness, it is beyond these authorities’ objectives to mandate what institutions’ business strategies should be (this lies with the institution’s management/board).

Thinking is still developing on how transition plans could support regulatory objectives.

Micro-prudential authorities around the world are increasingly exploring how transition plans could support supervisory actions and could be incorporated into current regulations to foster the prudential framework. However, this effort is proceeding at different speeds and for different purposes across the globe. This appears driven by a number of factors including different mandates of prudential authorities and the inclusion of climate-related risks in their policies, and the purpose for which transition plans are being introduced (for transparency to shareholders or for risk management). For examples,

- Micro-prudential authorities in emerging markets and developing economies (EMDEs) may have different considerations from their counterparts in more developed countries. For those regulators, one consideration could be how central banks and supervisors in EMDEs can help less sophisticated financial institutions in those jurisdictions to develop their transition plans, ensuring consistency with transition pathways, and how that would translate into the strategy, risk management, governance, and market opportunities for these institutions.

10 Ibid.
11 NGFS (2022): Capturing risk differentials from climate-related risks.
12 Grantham Research Institute on Climate Change and the Environment (2022): Net zero transition plans A supervisory playbook for prudential authorities.
• For other micro-prudential authorities who supervise financial institutions with cross-jurisdictional operations, an additional consideration for transition plans could be the extent to which they should be embedded in home/host supervisory cooperation.

• Current discussions around transition plans generally revolve around larger financial institutions. As a result, some micro-prudential authorities are also considering how best to apply the proportionality principle as it relates to transition plans.

It could be expected that in the case of transition plans, financial regulators pursue the traditional policy of market neutrality so as to not alter the normal functioning of the financial system and that they adopt a strict prudential perspective, not including — in the most cases — supporting and mitigation policies.

The stocktake exercise did not reveal any common perspective amongst authorities on how transition plans could be relevant for prudential objectives. Transition plans could embed wider purposes such as supporting the transition to a low emission economy.

Key finding 5: There are some common elements to all transition plans which are relevant to assessing safety and soundness

Information contained in common elements of transition plans, such as governance, strategy, risk management and metrics, can help regulators understand how firms meet relevant BCPs, ICPs, as well as BCBS and IAIS guidance as it relates to financial institutions’ management of climate-related risks, including their assessment of inherent strategic risks associated with their transition strategies.

i. Business model/strategy

Transition plans could be a relevant source of information to supervise the resilience of the business model, which depends, in general, on the financial institution’s strategy and, in particular, on the impact of climate-related risks. Therefore, a core common element for supervisory actions is the need to understand the institution’s business model, strategy and the risk exposure toward climate change and the transition over the short, medium and long-term.

ii. Risk management and metrics

Transition plans should set out how the impact of climate-related risks are embedded into the financial institution’s strategy and risk management framework, including information on the tools and processes used to make decisions in order to provide micro-prudential authorities with an understanding of the institution’s risk appetite for climate-related risks.

Transition plans can provide micro-prudential authorities with a more detailed understanding of institutions’ approaches to managing climate-related risks over the short-, medium-, and long-term, including their assumptions around transition scenarios and relevant transition pathways. They can also provide insight into how the institutions plan on achieving their climate-related targets, if one was adopted either voluntarily or mandated through legislation. This would be relevant to authorities as these plans, if misaligned with the current external and operating environment, or trajectories of institution’s clients, or implemented poorly, could lead to reputational or litigation risks and, in severe instances, affect the institutions’ safety and soundness.

iii. Governance

Disclosure of effective governance framework to shareholders, in terms of processes and structures, and clearly defining roles, responsibilities and remuneration, allows a robust evaluation of the strategy design and execution risk (GFANZ, UK TPT, US SEC rule, UNPRI). The information included in the transition plan can also be relevant to promote the accountability of financial institutions to their shareholders in terms of mapping, monitoring and controlling of risks (UNEPFI).

iv. Wider regulatory/financial stability objectives

Transition plans can also provide additional information relevant to a micro- and macro-prudential authority’s objectives. For example, transition plans can help authorities to examine and understand on a macro-level, the economic implications of climate-related risks (e.g., first order impacts) both on financial institutions and the overall financial sector. They can help authorities identify negative externalities or feedback loops from institutions’
decisions that, in aggregate, can affect the real economy and climate adaptation. These in turn, can further impact the institutions’ and financial sector’s exposure to climate-related risks (e.g., second-order impacts).

These common information points could inform the design of transition planning frameworks regardless of their thematic category or whether they are adopted by the micro-prudential authority, securities regulators, financial/climate reporting authority or alternate.

Transition plans can facilitate institutions' strategic thinking around managing their climate-related risks. As part of their supervisory risk assessment process, micro-prudential authorities have the ability to obtain this information which would be developed as part of transition planning from financial institutions. There is currently no guidance on the extent to which a micro-prudential authority could or should mandate transition plans to obtain the specific information required in line with their objectives. The driver and context behind an institution's transition plan will play a key role in driving supervisory expectations and risk management considerations, as set out in the diagram below.

Key finding 6: The role that micro-prudential authorities play needs to be situated in the context of the actions of other financial and non-financial regulators rather than acting in isolation.

There needs to be collaboration across financial regulatory as well as with real economy authorities, and between jurisdictions, to ensure interoperability of transition plans and reduce regulatory fragmentation and related burden on firms and prevent “arbitrage” of different emissions regulations and different interpretations of a group transition plan amongst different entities. Efforts by international organisations such as the FSB, BCBS, IAIS, IOSCO, ISSB, and OECD can help to harmonize such standards.

The NGFS identified a number of potential uses for the information within transition plans vis-à-vis financial regulators’ different objectives:
**Micro-prudential authority:**
Transition plans can enable monitoring of a financial institution’s short- and long-term strategy to manage climate-related risks and understand how different transition pathways can affect their continued safety and soundness.

They can help financial institutions demonstrate that they are aware of, and prepared for, the potential adverse impacts from inaction, delayed action or misalignment in transition.

Transition planning and the production of transition plans can also help financial institutions to thoroughly assess the structural changes that may occur within the industries the institutions are exposed to, according to the transition pathways compatible with the policy objectives and legal framework of the jurisdiction.

**Financial Stability/Macro-prudential authority:**
Transition plans can enable an understanding of how different transition pathways could affect the macroeconomy and the stability of the wider financial system. They can be a valuable input to understand systemic aspects of climate-related risk and related trends and gain consolidated view across the system, and feed information for future systemic climate-related risk monitoring tools.

**Securities or market conduct regulator:**
Public disclosure of transition plans can enable financial and non-financial firms to communicate the future direction and contribution of these institutions to advancing the transition, as these could have a material impact on business strategies and risk profiles and hence enterprise value.

The requirement to develop and disclose such plans works to increase transparency on the risks to which the financial institution is exposed and will ensure that these institutions proactively review, also in relation to the transition objectives of the jurisdiction, whether their strategies sufficiently incorporate ESG-related considerations, thereby mitigating reputational risks or risks arising from rapidly changing market sentiment as well.

**Government (via legislation):**
Transition plans enable monitoring of the financial sector’s role in the transition, namely if and how financial institutions are facilitating the flow of finance to support businesses and households in reducing their GHG emissions and meeting specific net zero targets.

An orderly transition mitigates the effect of climate change and the potential adverse financial impacts to the financial system. Transition plans should take national climate commitments into account and set concrete and tangible interim targets to facilitate action-taking.
6. Next steps

Following the overall conclusion and key findings, the NGFS will take forward actions in two broad areas: The first relates to the NGFS’s engagement with international standard setting bodies (SSBs) and the second relates to further work the NGFS will undertake.

1. Engagement with relevant international authorities and standard setters: Given the different scope of transition plans, as well as their potential relevance to the micro-prudential authorities, the NGFS will engage standard setting bodies, such as the FSB, BCBS, IAIS, and IOSCO, so that they can advance their respective work on transition plans and planning in a coordinated manner.

2. Further actions by the NGFS: Based on the findings of Phase 1, the NGFS will also take forward additional work to advance the discussion on the relevance of transition plans and planning to micro-prudential authorities’ mandate, supervisory toolkit, and the overall prudential framework.
Acknowledgments

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## Annex 1 – List of literature and transition plan frameworks reviewed

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<td>BCBS (2022)</td>
<td>Principles for the effective management and supervision of climate-related financial risks</td>
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<tr>
<td>CDP (2021)</td>
<td>Climate Transition Plans: Discussion Paper</td>
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<tr>
<td>Climate Action 100+ (2022)</td>
<td>Net Zero Company Benchmark</td>
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<td>Climate Policy Initiative (2022)</td>
<td>What Makes a Transition Plan Credible?</td>
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<td>Climate Safe Lending Framework / UN PRI (2021)</td>
<td>The Good Transition Plan</td>
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<tr>
<td>Financial Stability Board (2022)</td>
<td>Report on Supervisory and Regulatory Approaches to Climate-related Risks</td>
</tr>
<tr>
<td>GFANZ (2022)</td>
<td>Financial Institutions Net-Zero Transition Plans</td>
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<td>INSPIRE-GRI (2022)</td>
<td>A supervisory playbook for prudential authorities</td>
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<td>International Sustainability Standards Board (2022)</td>
<td>Exposure Draft IFRS S2 Climate-related Disclosures</td>
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<tr>
<td>Investor Group Climate Change (2022)</td>
<td>Corporate Climate Transition Plans: A guide to investor expectations</td>
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<td>SBTi (2022)</td>
<td>Foundations for Science-based Net-zero Target Setting in the Financial Sector</td>
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<tr>
<td>Securities Exchange Commission (2022)</td>
<td>SEC Proposes Rules to Enhance and Standardize Climate-Related Disclosures for Investors</td>
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<td>UK Transition Plan Taskforce (2022)</td>
<td>Call for Evidence Report</td>
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<td>UNEP-FI (2021)</td>
<td>High-Level Recommendations for Credible Net-Zero Commitments from Financial Institutions</td>
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